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BRITISH COLUMBIA AND MEXICO
THE TRILATERAL FREE TRADE PROPOSAL

A DISCUSSION PAPER

BACKGROUND

On June 10, 1990, U.S. President Bush and Mexican President Salinas endorsed the objective of a comprehensive free trade agreement between their two countries. An announcement of formal trade talks between Mexico and the U.S. was not expected until December, 1990, but the two countries accelerated their timetable for bilateral free trade negotiations and made the announcement in mid-August, 1990.

On September 24, 1990, the Honourable John Crosbie, federal Minister for International Trade, announced that the Government of Canada had expressed to the U.S. and Mexico its desire to participate in the negotiations with a view to negotiating a trilateral free trade agreement.

On September 25, 1990, President Bush wrote Congress seeking approval for authority to negotiate a "fast-track" trade deal with Mexico and Canada, similar to that which was granted for the negotiations leading to the Canada-U.S. Free Trade Agreement (FTA).

The Government of Canada has suggested it will follow a two-step process. The first step involves Canada, Mexico, and the U.S. participating in preliminary consultations to examine the scope, elements and procedures that could form the basis for trilateral free trade negotiations. The first of these preliminary talks took place in Houston, Texas, on October 16, 1990.

Should these preliminary consultations prove successful, the second step, formal free trade negotiations, could be initiated as early as the Spring of 1991. If agreement cannot be reached by the three countries during the preliminary talks, the federal government has indicated that it is prepared to leave the negotiating table and see the U.S. and Mexico pursue bilateral free trade negotiations.

BRITISH COLUMBIA-MEXICO TRADE RELATIONSHIP

A trade pact linking the U.S., Mexico and Canada would create a single market of almost 360 million people and a combined economy of about $6 trillion.

Although Mexico is Canada's

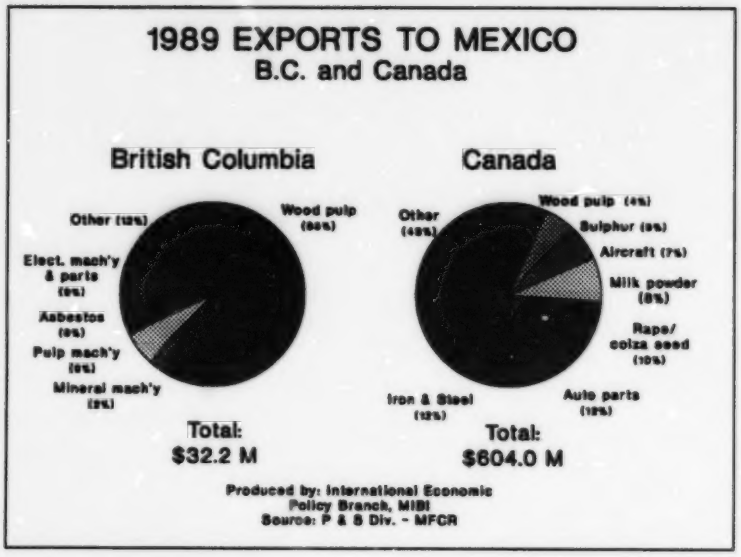
most important trade partner in Latin America, economic ties between the two countries are relatively modest.

Overall, Mexico is Canada's 17th most important export destination, accounting for $604 million worth of Canadian exports in 1989. Total trade between Mexico and Canada was worth $2.3 billion in 1989.

Mexico has traditionally held a trade surplus vis-a-vis Canada, and in 1989 this trend continued as Mexico had a trade surplus of $1.1 billion.

At present, British Columbia's trade with Mexico is minimal. In 1989, the province exported $32 million worth of goods to Mexico, making it the province's 26th largest export market overall. British Columbia's top exports to Mexico in 1989 were pulp (which made up two-thirds of the province's total exports to Mexico), electrical machinery, equipment and parts, asbestos, and machinery for pulp and mineral production.

However, past trade trends may not tell us much about future prospects. The Mexican government has taken significant steps over the past few years to open up the Mexican market to foreign trade and investment. The high tariffs and import licensing systems which previously



impeded British Columbia's trade with Mexico have been significantly liberalized, and further reductions are expected as a result of Mexico's participation in the GATT Multilateral Trade Negotiations (MTN).

In addition, Mexican economic growth is forecast to outpace growth rates of both Canada and the U.S., therefore it is an increasingly richer market.

Thus, free trade with Mexico may create some attractive potential market opportunities for British Columbia exporters in such diverse areas as newsprint, telecommunications equipment and services, mineral extraction and processing equipment and services, and tourism development.

Roughly 80% of Mexico's exports to Canada already arrive duty free. While freer trade with Mexico may put pressure on some sectors in British Columbia, these same sectors are in a much stronger position to cope with this import competition, having undergone adjustment as a result of increased multi-lateral and bilateral trade liberalization.

Insofar as the U.S. and Mexico have already committed themselves to establishing a bilateral free trade pact, British Columbia's competitive advantage under the Canada-U.S. FTA may be eroded if Mexico negotiates similar preferential treatment. On the other hand, if Canada is at the negotiating table, it may have the chance to influence the agenda for the negotiations and perhaps even find areas where Mexico and Canada could work together to achieve common trade goals.

POSSIBLE IMPACTS OF A TRILATERAL FREE TRADE AGREEMENT

Whether or not Canada participates in the U.S.-Mexico free trade negotiations, there will likely be some increased competition for British Columbia exporters in the U.S. and Mexican markets as well as some risk of investment diversion to Mexico. A free trade agreement with Mexico could affect British Columbia in any of the following five ways:

1) Increased export competition in the U.S. market - A U.S.-Mexico FTA would give Mexican producers special access to the U.S. market very similar to the access Canada gained under its FTA with the U.S.

However, based on a preliminary provincial government assessment, it appears there will be few serious competitive pressures for British Columbia industries currently exporting to the U.S., as a result of a U.S.-Mexico bilateral FTA or a Mexico-Canada-U.S. trilateral FTA. At this early stage, there is also little evidence that Canada's participation in the Mexico-Canada-U.S. free trade negotiations will significantly improve British Columbia's competitive position in the U.S. market vis-a-vis Mexican products.

2) Increased import competition in British Columbia - Should Canada choose to participate in a trilateral free trade agreement with Mexico and the U.S., certain domestic industries may face some competitive pressures due to the increased number of Mexican products and services entering the Canadian market at preferential rates. Sectors likely to be affected include the horticultural and textile/clothing industries, although these industries are already adjusting to international competitive pressures.

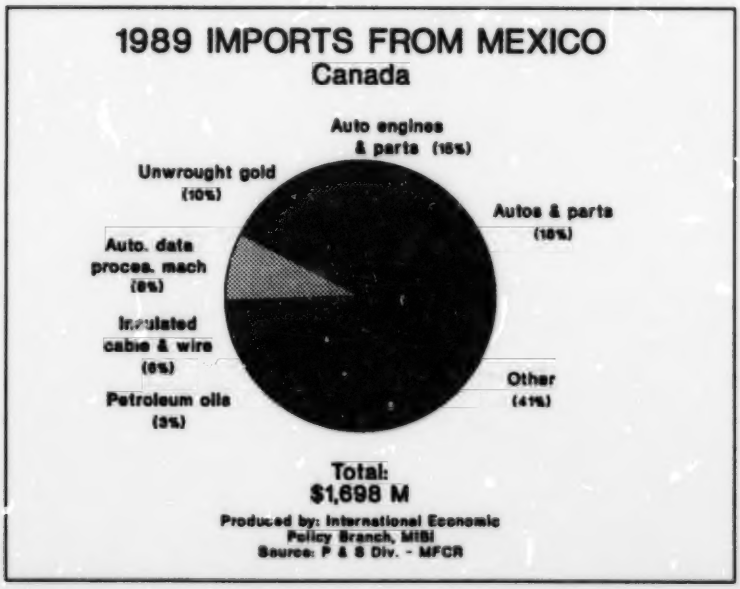
3) Increased export opportunities for British Columbia in Mexico - British Columbia may experience a modest increase in export opportunities in Mexico as a result of:

a) Mexico's recent efforts to unilaterally lower tariff and non-tariff barriers;

b) the trade liberalization which may occur in the Mexican market as a result of the conclusion of the GATT MTN; and

c) the trade liberalization which would result from a trilateral free trade agreement.

4) Increased export competition in the Mexican market - A bilateral free trade agreement between Mexico and the U.S. would give U.S. producers preferential access to the Mexican market. This, in turn, could negatively impact on the competitiveness of Canadian exporters in the Mexican market.


1989 IMPORTS FROM MEXICO
Canada
Auto engines & parts (16%)
Unwrought gold (10%)
Autos & parts (16%)
Auto. data proces. mach (8%)
Insulated cable & wire (6%)
Petroleum oils (3%)
Other (41%)
Total: $1,698 M
Produced by: International Economic Policy Branch, MIBI
Source: P & S Div. - MFCR

5) Possible investment diversion - Whether or not Canada participates in the U.S.-Mexico free trade negotiations, there is some risk of current and potential investment diversion from British Columbia to the U.S. and Mexico. While in many cases British Columbia will remain an attractive location for offshore investors, the lure of British Columbia's enhanced U.S. market access under the FTA will have less significance if Mexico is able to offer investors the same enhanced access to the U.S. market.

BRITISH COLUMBIA'S APPROACH TO CANADA-U.S.-MEXICO FREE TRADE

British Columbia has traditionally been a strong supporter of efforts to liberalize international trade (e.g., the Canada-U.S. FTA, and the GATT multilateral trade negotiations), because it is highly dependent on exports for its economic well-being.

However, unlike the U.S., the countries of the Pacific Rim, or the European Community, Mexico is not currently an important export destination for the Province. Mexico's recent economic liberalization efforts may, however, make it a much more desirable market in the future.

While the Province supports the liberalization of world trade, the key question to be asked is: do we know enough about the potential impacts of free trade with Mexico to proceed with these negotiations?

While there may be some merit in proceeding, the Province nevertheless wishes to study the trilateral free trade initiative carefully before committing its support to it. At this point, there is very little quantitative evidence available as to the costs or benefits of a North American free trade agreement.

The potential for a North American free trade zone raises a number of fundamental questions which must be addressed by British Columbians. For example:

- Can British Columbia's interests best be served from within a North American trade bloc or from without?
- Will a North American free trade agreement result in trade creation or trade diversion?
- What will be the long term impact on the international trading system of such a regional trade arrangement?
- What will be the benefits to British Columbia from such a trade arrangement? Will they outweigh the costs or adjustments that may be required in the province?

The Government of British Columbia has always attached a high priority to eliciting the views of the Province's private sector before proceeding with any major trade initiatives. For instance, the Province undertook a comprehensive series of private sector consultations on both the bilateral free trade negotiations with the U.S. and on the Uruguay Round of GATT multilateral trade negotiations.

British Columbia intends to take the time necessary to consult and to analyze the impacts and potential benefits of trilateral free trade on the Province. Only when this process has been completed will the Province have the necessary information to develop its recommendations to the federal government, and officially communicate British Columbia's position on the negotiations.

INTERNATIONAL ECONOMIC POLICY BRANCH

TRADE WITH MEXICO

EXPORTS FROM BRITISH COLUMBIA

COMMODITIES	1989 $ millions	1988 $ millions	88/89 % change
Wood pulp	21.1	33.5	-37
Elect. mach., equip & parts	2.7	0.7	286
Asbestos	2.1	1.2	75
Other	6.4	7.5	-15
TOTAL (All Commodities)	32.3	42.9	-25

TOTAL EXPORTS FROM CANADA

COMMODITIES	1989 $ millions	1988 $ millions	88/89 % change
Iron & steel	71.3	38.2	87
Auto parts & accessories	71.0	50.3	41
Rape or colza seeds	59.3	54.3	9
Milk powder	45.9	42.0	9
Helicopters	39.9	4.4	807
Other	316.6	299.8	6
TOTAL (All Commodities)	604.0	489.0	24

IMPORTS INTO CANADA

COMMODITIES	1989 $ millions	1988 $ millions	88/89 % change
Auto parts & accessories	224.1	179.6	25
Egine parts	215.9	217.0	-1
Gold	172.1	69.7	147
Auto. data proc. machines	140.7	84.7	66
Insulated wire	98.5	106.9	-8
Other	847.1	673.3	26
TOTAL (All Commodities)	1698.4	1331.2	28

Source: Planning & Statistics Division, Ministry of Finance & Corporate Relations